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No. 93-450

In the Supreme Court of the United States

OCTOBER TERM, 1993

JAMES ALBERT COONES, PETITIONER

v.

FEDERAL DEPOSIT INSURANCE CORPORATION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether the court of appeals correctly determined that under 11 U.S.C. 552 the Federal Deposit Insurance Corporation (FDIC) had a security interest in property acquired after the filing of a bankruptcy petition because that property was produced with the proceeds of pre-petition property in which the FDIC had a security interest.

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OPINIONS BELOW

The opinions of the court of appeals (Pet. App. 1a-7a, 8a-28a) are reported at 996 F.2d 250 and 954 F.2d 596. The opinion of the district court (Pet. App. 29a-67a) is unreported. The opinions of the bankruptcy court (Pet. App. 68a-78a, 79a-80a) are also unreported.

JURISDICTION

The judgment of the court of appeals was entered on June 21, 1993. The petition for a writ of certiorari was filed on September 17, 1993. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioner, a Wyoming cattleman and farmer, and his wife (the debtors) jointly obtained two loans in 1986 totaling approximately $470,000 from Stockmen's Bank & Trust Company. Pet App. 31a. In connection with those loans, they executed two promissory notes and two security agreements. The security agreements gave Stockmen's a secured interest in:

> All farm products of the [debtors], whether now owned or hereafter acquired including but not limited to (i) all poultry and livestock and their young, products thereof and produce thereof, (ii) all crops, whether annual or perennial, and the products thereof * * * [and]:
>
> All inventory of cattle, horses, and all other livestock, all farm products of cattle, horses, and all farm equipment and machinery, * * * farm products, * * * crops, crop inventory and crop farm products * * * now owned or hereafter acquired.

Id. at 10a-11a.

On October 20, 1988, the debtors filed a petition in the United States Bankruptcy Court for the District of Wyoming, seeking relief under Chapter 11 of the Bankruptcy Code. At the time they filed their petition, the debtors did not submit all of the schedules and statements required under Bankruptcy Rule 1007, nor did they ask for an extension of time to file them.[1] In particular, the debtors did not file a

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[1] Bankruptcy Rule 1007(b)(1) requires the debtor in a Chapter 11 case to file schedules of assets and liabilities, a schedule of current income and expenditures, a statement of

completed schedule of exemptions until November 16, 1988, 27 days after the petition was filed.[2]

In the schedule of exemptions they ultimately filed, the debtors listed as exempt property 75 percent of the livestock they acquired after 1986 and 75 percent of the crops grown after 1986. They asserted that this property was exempt as personal service earnings under Wyoming law. Pet. App. 11a-12a. No timely objection to this exemption claim was filed by the Federal Deposit Insurance Corporation (FDIC) or any other interested party. See 11 U.S.C. 522(*l*); Bankr. R. 4003(b).

2. The FDIC was appointed receiver of Stockmen's in 1987. In that capacity, the FDIC was the holder of the notes and security agreements that the debtors had executed in favor of Stockmen's in 1986. Pet App. 31a. In February, 1989, the debtors applied to the bankruptcy court to avoid the FDIC's liens on the crops and livestock as to which they had claimed an exemption. See 11 U.S.C. 522(f). Also in February, 1989, the FDIC filed a motion to prohibit the debtors' use of cash collateral. See Pet. App. 12a; 11 U.S.C. 363(e).

The bankruptcy court denied the debtors' claimed exemptions, despite the lack of a timely objection by the FDIC, holding that the exemptions had no basis in

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financial affairs, and a statement of executory contracts. Under Rule 1007(c), these schedules and statements must "be filed with the petition * * *, or if the petition is accompanied by a list of all the debtor's creditors and their addresses, within 15 days thereafter."

[2] Under Bankruptcy Rule 4003(a), "[a] debtor shall list the property claimed as exempt under § 522 of the Code on the schedule of assets required to be filed by Rule 1007."

state law. Pet. App. 12a. The court also denied the FDIC's motion to prohibit use of cash collateral with respect to the FDIC's interest in the debtors' crops, holding that the FDIC did not have an enforceable security interest in that property. *Id.* at 12a-13a, 68a-78a.

3. On cross-appeals, the district court certified to the Wyoming Supreme Court the question whether state law permitted the debtors to exempt livestock acquired and crops grown after 1986 as "personal service earnings." Pet. App. 13a. The Wyoming Supreme Court declared that the exemptions were not valid as personal service earnings under state law. *Coones* v. *FDIC*, 796 P.2d 803, 804, 806 (Wyo. 1990). Based on the Wyoming Supreme Court's decision, the district court held that the debtors were not entitled to the exemptions, despite the FDIC's failure to file a timely objection to their exemption claims. Pet. App. 13a-14a.

In a separate order, the district court held that the FDIC had a perfected security interest in the debtors' post-petition crops. Pet. App. 29a-67a. The court rejected the debtors' argument that 11 U.S.C. 552(a) extinguished the FDIC's lien on the post-petition crops. The court determined that, because "the [debtors] used the proceeds from the FDIC's pre-petition crops to create the post-petition property," the post-petition property constituted "proceeds" in which the FDIC retained a secured interest pursuant to 11 U.S.C. 552(b). Pet. App. 61a.[3]

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[3] Section 552 (11 U.S.C.) provides:

(a) Except as provided in subsection (b) of this section, property acquired by the estate or by the debtor after the

4. The court of appeals affirmed. Pet. App. 8a-28a.[4] It held that the FDIC's failure to object to the debtors' exemption claim did not "preclude the bankruptcy court's exercise of its authority to deny an exemption that ha[d] no legal basis." *Id.* at 15a. It also held that the FDIC had a perfected security interest in the debtors' post-petition crops under 11 U.S.C. 552(b). Pet. App. 17a-25a.

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commencement of the case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case.

(b) Except as provided in sections 363, 506(c), 522, 544, 545, 547, and 548 of this title, if the debtor and an entity entered into a security agreement before the commencement of the case and if the security interest created by such security agreement extends to property of the debtor acquired before the commencement of the case and to proceeds, product, offspring, rents, or profits of such property, then such security interest extends to such proceeds, product, offspring, rents, or profits acquired by the estate after the commencement of the case to the extent provided by such security agreement and by applicable nonbankruptcy law, except to any extent that the court, after notice and a hearing and based on the equities of the case, orders otherwise.

[4] While the cross-appeals were pending in the district court, the bankruptcy court denied confirmation of the debtors' proposed Chapter 11 plan. Subsequently, the bankruptcy court denied the debtors' motion to convert to a Chapter 12 proceeding. On March 29, 1990, the bankruptcy court granted the creditors' motion to dismiss the Chapter 11 proceeding, but gave the debtors ten days to elect to convert to a case under Chapter 7. Petitioner's wife converted to a Chapter 7 case, but petitioner did not. Instead, he appealed the order dismissing the case. That appeal is pending.

5. The debtors sought review of both holdings by filing a petition for a writ of certiorari in this Court. In light of this Court's intervening decision in *Taylor* v. *Freeland & Kronz*, 112 S. Ct. 1644 (1992), the FDIC agreed with petitioners that the court of appeals had erred in holding that the FDIC was entitled to object to their exemption claim, despite the FDIC's failure to file a timely objection to that claim. The FDIC accordingly suggested that, with respect to that issue, this Court grant the petition, vacate the judgment of the court of appeals, and remand the case to the court of appeals for further consideration in light of *Freeland & Kronz*. The Court did so. 113 S. Ct. 31 (1992). The Court subsequently denied petitioner's motion for clarification of the remand order. 113 S. Ct. 402 (1992).

6. On remand, the court of appeals reversed itself on the issue as to which the FDIC had acquiesced in the granting of the petition for certiorari, holding, in light of *Freeland & Kronz*, that the FDIC's failure to file a timely objection barred it from objecting to petitioner's exemption claim. The court adhered, however, to its prior holding that the FDIC had a security interest in post-petition crops produced with the proceeds of pre-petition property in which the FDIC had held a security interest. Pet. App. 3a, 7a.

ARGUMENT

Petitioner challenges the court of appeals' holding that under 11 U.S.C. 552(b) the FDIC had a perfected security interest in crops acquired after the petition for bankruptcy was filed. Pet. 11-17. That contention does not warrant further review.

Section 552 of the Bankruptcy Code addresses the effect of pre-petition security agreements on property acquired after the petition has been filed. Section 552(a) provides that "[e]xcept as provided in subsection (b) of this section, property acquired by the estate or by the debtor after the commencement of the case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case." 11 U.S.C. 552(a). Section 552(b), in turn, provides that, with exceptions not pertinent here:

> [I]f the debtor and an entity entered into a security agreement before the commencement of the case and if the security interest created by such security agreement extends to property of the debtor acquired before the commencement of the case and to proceeds * * * of such property, then such security interest extends to such proceeds * * * to the extent provided by such security agreement and by applicable non-bankruptcy law.

11 U.S.C. 552(b). Thus, under Section 552 an entity's security interest in pre-petition property extends to post-petition property that constitutes "proceeds" of the pre-petition property, if the security agreement between the entity and the debtor so provides.

It is undisputed in this case that the security agreements between the debtors and Stockmen's, to which the FDIC succeeded, provided for a security interest in the proceeds of the debtors' crops. Furthermore, the district court found that petitioner and his wife "used the proceeds from the FDIC's pre-petition crops to create the post-petition property" in

which the FDIC claimed an interest. Pet. App. 61a. The court of appeals accepted that finding, observing that petitioner did not identify any evidence to contravene it. *Id.* at 26a-28a; see also *id.* at 9a-10a (applying a "clearly erroneous" standard of review to findings of fact). The court of appeals held that "because the post-petition crops were produced with the proceeds of debtors' pre-petition crops, proceeds in which the FDIC's security interest continued after initiation of bankruptcy proceedings, § 552 did not extinguish the FDIC's secured interest in the post-petition crops." *Id.* at 26a-27a.

The court of appeals' holding reflects a straightforward reading of Section 552(b). Under that reading, Section 552(b) applies when a security agreement covering pre-petition property creates a security interest in both the property and "proceeds" of that property. In that situation, Section 552(b) provides that the holder of the security interest retains an interest in such proceeds, even if those proceeds are acquired after commencement of the bankruptcy case. Having determined that the debtors' post-petition crops were created with the proceeds of pre-petition crops in which the FDIC had a security interest, the court of appeals correctly concluded that the FDIC retained an interest in the post-petition crops under Section 552(b).

Contrary to petitioner's suggestion, the court of appeals' conclusion does not conflict with the decision of any other court of appeals.[5] Moreover, the decision

[5] Petitioner contends (Pet. 15) that the decision of the court of appeals in this case "appears to conflict with the rationale underlying" *In re Bering Trader, Inc.*, 944 F.2d 500 (9th Cir. 1991), and *In re Jones*, 908 F.2d 859 (11th Cir. 1990). In those

of the court of appeals accords with decisions in other circuits involving similar facts. See *In re Bumper Sales, Inc.*, 907 F.2d 1430, 1439 (4th Cir. 1990); *J. Catton Farms, Inc.* v. *First Nat'l Bank*, 779 F.2d 1242, 1244, 1246-1247 (7th Cir. 1985); see also B. Clark, *The Law of Secured Transactions Under the Uniform Commercial Code* ¶ 6.04[1], at 6-55 (2d ed. 1988) ("[T]he term 'proceeds' should be read broadly—as in UCC § 9-306—to include after-acquired property, at least where inventory and accounts are concerned, there is no improvement in position, and tracing can be accomplished. This is nothing more than a post-petition substitution of collateral."). Further review is therefore not warranted.

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cases, however, the courts of appeals merely held—on facts quite different from those of this case—that the post-petition property at issue did not constitute "proceeds" of pre-petition property in which the creditor held a security interest. See *In re Bering Trader*, 944 F.2d at 501-502 (post-petition rent payments on a charter vessel were not "proceeds"); *In re Jones*, 908 F.2d at 860-861 (post-petition increase in cash surrender value of life insurance policy was not "proceeds"). These fact-specific holdings are inapposite here. For the same reason, the district court and bankruptcy court decisions upon which petitioner relies (Pet. 15) are also inapposite.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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